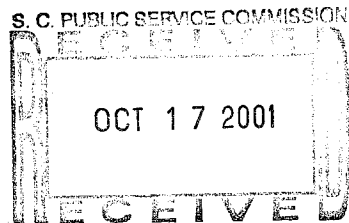


POSTED
W10-701

Application of Dowd Water Systems, Inc. requesting approval for the establishment of rates and charges for Emerald Shores and Isle of Pines in Lexington County



Docket No. 2001-181-W

RETURN DATE: OK DJ
SERVICE: OK DJ

***Testimony of
Steve W. Gunter
Audit Department***

Public Service Commission of South Carolina

1 Q. PLEASE STATE FOR THE RECORD YOUR NAME, BUSINESS ADDRESS
2 AND POSITION WITH THE PUBLIC SERVICE COMMISSION OF SOUTH
3 CAROLINA.

4 A. My name is Steve W. Gunter. My business address is 101
5 Executive Center Drive, Columbia, South Carolina. I am
6 employed by the Public Service Commission of South
7 Carolina as an Auditor.

8 Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND YOUR
9 EXPERIENCE.

10 A. I received a B.A. Degree in Interdisciplinary Studies
11 with a major in Accounting from the University of South
12 Carolina in 1980. I am a Certified Public Accountant,
13 certified in the State of South Carolina. I have 19
14 years of experience in the auditing profession. Eighteen
15 of those years have involved the ratemaking process.

16 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY INVOLVING DOWD
17 WATER SYSTEM'S, INC.?

18 A. The purpose of my testimony is to set forth in summary
19 form Staff's findings and recommendations resulting from
20 our examination concerning the above docket. These
21 findings and recommendations are set forth in the
22 exhibits of the Audit Department. The Dowd Water Systems
23 consists of three subdivisions which are Stephenson's

1 Lake, Emerald Shores, and Isle of Pines. Of the three
2 subdivisions, Stephenson's Lake is the only one that has
3 approved rates. The Company is asking the Commission to
4 approve rates for the other two subdivisions under this
5 docket.

6 Q. IN CONNECTION WITH YOUR TESTIMONY, DID YOU PREPARE OR
7 CAUSE TO BE PREPARED CERTAIN EXHIBITS?

8 A. Yes, The Audit Department Staff has prepared Exhibits A,
9 AB, AC and A-1 which are attached to my testimony.
10 Exhibit A presents the combined operations of the
11 Emerald Shores and Isle of Pines subdivisions. Exhibit
12 AB presents the operations of Emerald Shores and Exhibit
13 AC presents the operations of Isle of Pines.

14
15 Q. DO YOU HAVE ANY FURTHER EXPLANATION OF EXHIBITS A, AB,
16 AND AC?

17 A. Yes, the Audit Staff has prepared these exhibits in
18 compliance with the Commission's standard procedures as
19 to calculating income and operating margin for water and
20 wastewater companies. A brief description of Exhibits A,
21 AB and AC are as follows:

22 Column(1): Represents the Company's per book
23 operations for the test year ended December 31, 2000 as

1 filed by the Company in its application for the
2 requested increase. These numbers were verified by the
3 Staff as part of our review of the Company's books and
4 records.

5 Column(2): The Staff's Accounting and Pro Forma
6 Adjustments are detailed in this column. These
7 adjustments were made by the Audit Staff in order to
8 correct or normalize the Company's per book operations
9 and are detailed separately in Staff's Exhibit A-1.

10 Column(3): The Staff's computation of the
11 Company's normalized test year prior to the effect of
12 the proposed increase is detailed in this column of
13 Exhibits A, AB and AC.

14 Column(4): The Staff's adjustments for the
15 proposed increase as furnished by the Utilities
16 Department and all related tax and expense adjustments
17 that are associated with the proposed increase are
18 detailed in this column.

19 Column(5): The Staff's computation of the
20 Company's normalized test year after the effect of
21 accounting and pro forma adjustments and the effect of
22 the proposed increases and their associated tax and
23 expense adjustments are detailed in this column.

1 Q. WOULD YOU PLEASE ELABORATE ON THE CALCULATIONS IN
2 EXHIBIT A?

3 A. This exhibit shows the operating experience and
4 operating margin on a combined basis for Emerald Shores
5 and Isle of Pines subdivisions. As shown in column(1),
6 per book operations were used by Staff to compute "Net
7 Income For Return" of \$638. This was based on Operating
8 Revenue of \$6,960 less Operating Expenses of \$6,322. The
9 Staff computed an operating margin of 9.17%.

10 In Column(2), the Staff's Accounting and Pro Forma
11 adjustments are presented. These adjustments are shown
12 in more detail in Staff's Exhibit A-1 which is attached
13 to my testimony.

14 Column(3) presents per book operations as adjusted
15 by the Staff. After such adjustments, the Staff computed
16 a negative "Net Income For Return" of (\$1,145). This was
17 the result of Operating Revenues of \$6,960 less
18 Operating Expenses of \$8,105. By using the "Net Income
19 For Return" as adjusted, the Staff computed a negative
20 operating margin of (16.45)%.

21 Column(4) presents the Staff's adjustments
22 resulting from the proposed increase, as furnished by

1 the Utilities Department. These adjustments are also
2 detailed in Exhibit A-1.

3 Column(5) presents per book operations as adjusted
4 to normalize the test year and after the proposed
5 increase is added to revenue. As a result "Net Income
6 For Return" of \$8,886 was computed by the Staff. Such
7 income was based on Operating Revenue of \$19,248 less
8 Operating Expenses of \$10,362. By using the resulting
9 "Net Income For Return" of \$8,886 the Staff computed an
10 operating margin of 46.17%.

11 **Q. WOULD YOU PLEASE ELABORATE ON THE CALCULATIONS IN**
12 **EXHIBIT AB?**

13 **A.** This exhibit shows the operating experience and
14 operating margin for Emerald Shores Subdivision. As
15 shown in column (1), per book operations was used to
16 compute an "Operating Loss For Return" of (\$1,170). This
17 was based on operating revenues of \$4,080 less operating
18 expenses of \$5,250. The Staff computed an operating
19 margin of (28.68%).

20 In column 2, Staff's accounting and pro forma
21 adjustments are presented. These adjustments are shown
22 in more detail in Staff's Exhibit A-1.

1 Column(3) presents per book operations as adjusted by
2 the Staff. After such adjustments, the Staff computed a
3 negative "Net Income For Return" of (\$2,572). This was
4 the result of Operating Revenues of \$4,080 less
5 Operating Expenses of \$6,652. By using the "Net Loss For
6 Return" as adjusted, the Staff computed a negative
7 operating margin of (63.04)%.

8 Column(4) presents the Staff's adjustments for the
9 proposed increase, as furnished by the Utilities
10 Department. These adjustments are also detailed in
11 Exhibit A-1.

12 Column(5) presents per book operations as adjusted
13 to normalize the test year and after the proposed
14 increase is added to revenue. As a result "Net Income
15 For Return" of \$4,764 was computed by the Staff. Such
16 income was based on Operating Revenue of \$12,648 less
17 Operating Expenses of \$7,884. By using the resulting
18 "Net Income For Return" of \$4,764 the Staff computed an
19 operating margin of 37.67%.

20
21 Q. WOULD YOU PLEASE ELABORATE ON THE CALCULATIONS IN
22 EXHIBIT AC?

1 A. This exhibit shows the operating experience and
2 operating margin for Isle of Pines Subdivision. As shown
3 in column (1), per book operations was used to computed
4 a "Net Income For Return" of \$1,808. This was based on
5 operating revenues of \$2,880 less operating expenses of
6 \$1,072. The Staff computed an operating margin of
7 62.78%.

8 In column (2), Staff's accounting and pro forma
9 adjustments are presented. These adjustments are shown
10 in more detail in Staff's Exhibit A-1.

11 Column(3) presents per book operations as adjusted by
12 the Staff. After such adjustments, the Staff computed a
13 "Net Income For Return" of \$1,427. This was the result
14 of Operating Revenues of \$2,880 less Operating Expenses
15 of \$1,453. By using the "Net Income For Return" as
16 adjusted, the Staff computed an operating margin of
17 49.55%.

18 Column(4) presents the Staff's adjustments for the
19 proposed increase, as furnished by the Utilities
20 Department. These adjustments are also detailed in
21 Exhibit A-1.

22 Column(5) presents per book operations as adjusted
23 to normalize the test year and after the proposed

1 increase is added to revenue. As a result "Net Income
2 For Return" of \$4,122 was computed by the Staff. Such
3 income was based on Operating Revenue of \$6,600 less
4 Operating Expenses of \$2,478. By using the resulting
5 "Net Income For Return" of \$4,122 the Staff computed an
6 operating margin of 62.45%.

7
8 **Q. WOULD YOU PLEASE EXPLAIN STAFF'S PROPOSED ADJUSTMENTS**
9 **AS SHOWN IN EXHIBIT A-1?**

10 **A.** The Audit Staff proposed seven accounting and proforma
11 adjustments and one adjustment for the proposed
12 increase. In adjustment No.1 both the Staff and the
13 Company propose to adjust testing fees for the effect
14 of switching the responsibility of testing to an
15 outside contractor, effective April 1, 2001. The Staff
16 and the Company's adjustment allocated this cost to
17 Emerald Shores Subdivision based on the number of
18 customers in the Stephenson's Lake and Emerald Shores
19 Subdivisions, the two subdivisions covered under the
20 contract. Staff is of the opinion that an allocation
21 based on number of customers is more representative of
22 the actual cost to be incurred by each subdivision. The
23 total annual contract amount was \$13,236 of which

1 60.98% was allocated to Stephenson's Lake and 39.02% to
2 Emerald Shores based on 25 customers in the
3 Stephenson's Lake Subdivision and 16 customers in the
4 Emerald Shores Subdivision. The computation resulted in
5 an assignment of \$5,165 to Emerald Shores for testing
6 fees. Staff then eliminated the per book amounts
7 totaling \$2,486 for testing fees. Such Per Book fees
8 consisted of \$500 for testing, chemical expense
9 amounting to \$186 and operator fees in the amount of
10 \$1,800. The net adjustment totaled \$2,679. In
11 adjustment No. 2, the Staff and the Company propose to
12 adjust testing fees for the effect of switching the
13 responsibility to an outside contractor, effective in
14 2001 for the Isle of Pines Subdivision. The Company
15 booked \$499 in testing fees during the test year. The
16 cost to have the independent contractor perform such
17 services will be \$804 per year. The Staff considers the
18 \$305 increase in testing fees to be a known and
19 measurable change in expenses. In adjustment No. 3, The
20 Staff proposes to reduce Operating and Maintenance
21 expenses of the Emerald Shores Subdivision for a major
22 pump repair occurring during the test year. The Staff
23 proposes to capitalize this expenditure and depreciate

1 the cost over the pump repair's useful life of ten
2 years. In adjustment No. 4, The Staff and the Company
3 propose to depreciate the cost of a major pump repair
4 occurring outside the test year for the Emerald Shores
5 Subdivision. The Staff proposes to capitalize and
6 depreciate the repair over its useful life of ten years
7 while the Company proposes to amortize the cost over
8 three years. In adjustment No. 5, The Company proposes
9 to amortize the cost of replacing a pump which was
10 damaged when the county damaged water lines causing the
11 pump to over heat and burn-up. The Company proposes to
12 amortize the cost of the pump over two years and the
13 cost to repair the water lines over three years. The
14 Staff was informed that these costs may be reimbursed
15 by the county. The Staff does not believe that such
16 costs should be recovered from the Company's ratepayers
17 if such costs are to be reimbursed. In adjustment No.
18 6, The Staff and the Company propose to amortize rate
19 case expenses over three years. This has the effect of
20 normalizing the test year. In adjustment No. 7, The
21 Staff and the Company propose to true-up the gross
22 receipts tax assessment imposed by the Public Service
23 Commission. The Staff and the Company differed due to

1 Staff's use of a more up-to-date factor in the
2 calculation. In adjustment No. 8, The Staff and the
3 Company show the effect of the proposed increase in
4 rates. The updated gross receipts tax factor was used
5 by the Staff in computing Taxes Other Than Income
6 Taxes. Staff's income tax calculation was based on
7 taxable income after the Staff's adjustments.

8

9 Q. WOULD YOU PLEASE EXPLAIN WHY THE STAFF DID NOT COMPUTE
10 CUSTOMER GROWTH?

11 A. Beginning and ending customers both totaled 36 on a
12 combined basis, which included 16 customers for Emerald
13 Shores Subdivision and 20 customers for Isle of Pines.
14 Because there was no increase in the number of customers
15 during the test year for either Emerald Shores or Isle
16 of Pines, no customer growth was computed.

17 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

18 A. Yes, it does.

Dowd Water System's, Inc.
 Emerald Shores and Isle of Pines Subdivisions - Combined
 Operating Experience and Operating Margin
 Test Year Ended December 31, 2000

Description	(1) Per Books \$	(2) Accounting & Pro Forma Adjustments \$	(3) As Adjusted \$	(4) Proposed Increase \$	(5) After Proposed Increase \$
Operating Revenue:					
Service Revenue	6,960	0	6,960	12,288	(4) 19,248
Total Operating Revenues	<u>6,960</u>	<u>0</u>	<u>6,960</u>	<u>12,288</u>	<u>19,248</u>
Operating Expenses:					
Operating and Maintenance Expenses	5,934	1,166 (1)	7,100	0	7,100
General and Administrative Expenses	326	0	326	0	326
Depreciation & Amortization Expense	0	539 (2)	539	0	539
Taxes Other Than Income	62	78 (3)	140	138 (5)	278
Income Taxes	0	0	0	2,119 (6)	2,119
Total Operating Expenses	<u>6,322</u>	<u>1,783</u>	<u>8,105</u>	<u>2,257</u>	<u>10,362</u>
Net Operating Income	638	(1,783)	(1,145)	10,031	8,886
Customer Growth - See Note 1	0	0	0	0	0
Net Income For Return	<u>638</u>	<u>(1,783)</u>	<u>(1,145)</u>	<u>10,031</u>	<u>8,886</u>
Operating Margin	<u>9.17%</u>		<u>(16.45%)</u>		<u>46.17%</u>

NOTE 1: There was no customer growth during the test year.

NOTE 2: The Company had no interest expense during the test year.

Dowd Water System's, Inc.
 Emerald Shores Subdivision
 Operating Experience and Operating Margin
 Test Year Ended December 31, 2000

Description	(1) Per Books \$	(2) Accounting & Pro Forma Adjustments \$	(3) As Adjusted \$	(4) Proposed Increase \$	(5) After Proposed Increase \$
Operating Revenue:					
Service Revenue	4,080	0	4,080	8,568	(4) 12,648
Total Operating Revenues	<u>4,080</u>	<u>0</u>	<u>4,080</u>	<u>8,568</u>	<u>12,648</u>
Operating Expenses:					
Operating and Maintenance Expenses	5,059	861 (1)	5,920	0	5,920
General and Administrative Expenses	150	0	150	0	150
Depreciation & Amortization Expense	0	495 (2)	495	0	495
Taxes Other Than Income	41	46 (3)	87	96	(5) 183
Income Taxes	0	0	0	1,136	(6) 1,136
Total Operating Expenses	<u>5,250</u>	<u>1,402</u>	<u>6,652</u>	<u>1,232</u>	<u>7,884</u>
Net Operating Income	(1,170)	(1,402)	(2,572)	7,336	4,764
Customer Growth - See Note 1	0	0	0	0	0
Net Income For Return	<u>(1,170)</u>	<u>(1,402)</u>	<u>(2,572)</u>	<u>7,336</u>	<u>4,764</u>
Operating Margin	<u>(28.68%)</u>		<u>(63.04%)</u>		<u>37.67%</u>

NOTE 1: There was no customer growth during the test year.

NOTE 2: The Company had no interest expense during the test year.

Dowd Water System's, Inc.
Isle of Pines Subdivision
Operating Experience and Operating Margin
Test Year Ended December 31, 2000

Description	(1) Per Books	(2) Accounting & Pro Forma Adjustments	(3) As Adjusted	(4) Proposed Increase	(5) After Proposed Increase
	\$	\$	\$	\$	\$
Operating Revenue:					
Service Revenue	2,880	0	2,880	3,720 (4)	6,600
Total Operating Revenues	<u>2,880</u>	<u>0</u>	<u>2,880</u>	<u>3,720</u>	<u>6,600</u>
Operating Expenses:					
Operating and Maintenance Expenses	875	305 (1)	1,180	0	1,180
General and Administrative Expenses	176	0	176	0	176
Depreciation & Amortization Expense	0	44 (2)	44	0	44
Taxes Other Than Income	21	32 (3)	53	42 (5)	95
Income Taxes	0	0	0	983 (6)	983
Total Operating Expenses	<u>1,072</u>	<u>381</u>	<u>1,453</u>	<u>1,025</u>	<u>2,478</u>
Net Operating Income	1,808	(381)	1,427	2,695	4,122
Customer Growth - See Note 1	0	0	0	0	0
Net Income For Return	<u>1,808</u>	<u>(381)</u>	<u>1,427</u>	<u>2,695</u>	<u>4,122</u>
Operating Margin	<u>62.78%</u>		<u>49.55%</u>		<u>62.45%</u>

NOTE 1: There was no customer growth during the test year.

NOTE 2: The Company had no interest expense during the test year.

Dowd Water System's, Inc.
Isle of Pines and Emerald Shores Subdivisions
Explanation of Accounting and Pro Forma Adjustments
Test Year Ended December 31, 2000

Revenues and Expenses	(1)	(2)	(3)
Description	O&M Expenses	Depreciation & Amortization Expense	Taxes Other Than Income
	\$	\$	\$
(1) The Staff and the Company propose to adjust testing fees for the effect of switching the responsibility to an outside contractor, effective April 1, 2001. The total annual contract amount was \$13,236 of which 60.98% was allocated to Stephenson's Lake and 39.02% to Emerald Shores based on 25 customers in the Stephenson's Lake Subdivision and 16 customers in the Emerald Shores Subdivision. The Staff and the Company then eliminated the Per Book amounts for testing fees in the amount of \$ 2,486. (A)			
Per Staff - Combined	2,679		
Per Staff - Emerald Shores	2,679		
Per Staff - Isle of Pines	0		
Per Company - Combined	2,679		
Per Company - Emerald Shores	2,679		
Per Company - Isle of Pines	0		
(2) The Staff and the Company propose to adjust Isle of Pines testing fees for the effect of switching the responsibility to an outside contractor after the test year ended. The adjustment is a known and measurable change.(A)			
Per Staff - Combined	305		
Per Staff - Emerald Shores	0		
Per Staff - Isle of Pines	305		
Per Company - Combined	305		
Per Company - Emerald Shores	0		
Per Company - Isle of Pines	305		
(3) The Staff proposes to reduce O&M expenses of the Emerald Shores Subdivision for a major pump repair occurring during the test year. Staff proposes to capitalize this expenditure and depreciate it over the pump's useful life of ten years. (A&U)			
Per Staff - Combined	(1,818)	182	
Per Staff - Emerald Shores	(1,818)	182	
Per Staff - Isle of Pines	0	0	
Per Company - Combined	0	0	
Per Company - Emerald Shores	0	0	
Per Company - Isle of Pines	0	0	

Dowd Water System's, Inc.
Isle of Pines and Emerald Shores Subdivisions
Explanation of Accounting and Pro Forma Adjustments
Test Year Ended December 31, 2000

Revenues and Expenses	(1)	(2)	(3)
Description	O&M Expenses	Depreciation & Amortization Expense	Taxes Other Than Income
	\$	\$	\$
(4) The Staff proposes to depreciate the cost of a major pump repair occurring outside the test year for the Emerald Shores Subdivision. The Staff proposes to capitalize and depreciate the repair over its useful life of ten years while the Company proposes to amortize the cost over three years. (A&U)			
Per Staff - Combined		269	
Per Staff - Emerald Shores		269	
Per Staff - Isle of Pines		0	
Per Company - Combined		435	
Per Company - Emerald Shores		435	
Per Company - Isle of Pines		0	
(5) The Company proposes a three year amortization of the cost of repairing a water line damaged by the county. The Company proposes a two year amortization of the cost of replacing a pump that overheated and was ruined when such line was damaged. The Staff did not accept the adjustment because the Company may be reimbursed by the county for such damage. (A&U)			
Per Staff - Combined		0	
Per Staff - Emerald Shores		0	
Per Staff - Isle of Pines		0	
Per Company - Combined		1,538	
Per Company - Emerald Shores		0	
Per Company - Isle of Pines		1,538	

Dowd Water System's, Inc.
Isle of Pines and Emerald Shores Subdivisions
Explanation of Accounting and Pro Forma Adjustments
Test Year Ended December 31, 2000

Revenues and Expenses	(1)	(2)	(3)
Description	O&M Expenses	Depreciation & Amortization Expense	Taxes Other Than Income
	\$	\$	\$
(6) The Staff and the Company propose to amortize rate case expenses over three years. The Staff and Company are allocating one-third of this amount to Stephenson's Lake and one-third each to Emerald Shores and Isle of Pines subdivisions. Staff allocated the cost evenly based on the assumption that the time and expense to prepare each case would be approximately the same. (A)			
Per Staff - Combined		88	
Per Staff - Emerald Shores		44	
Per Staff - Isle of Pines		44	
Per Company - Combined		88	
Per Company - Emerald Shores		44	
Per Company - Isle of Pines		44	
(7) The Staff and the Company propose to true-up the gross receipts tax assessment imposed by the Public Service Commission. The Staff and the Company's adjustment differed due to the use of a more up-to-date factor by the Staff. (A)			
Per Staff - Combined			78
Per Staff - Emerald Shores			46
Per Staff - Isle of Pines			32
Per Company - Combined			78
Per Company - Emerald Shores			46
Per Company - Isle of Pines			32
Total Adjustments Per Staff - Combined	1,166	539	78
Total Adjustments Per Staff - Emerald Shores	861	495	46
Total Adjustments Per Staff - Isle of Pines	305	44	32
Total Adjustments Per Company - Combined	2,984	2,061	78
Total Adjustments Per Company - Emerald Shores	2,679	479	46
Total Adjustments Per Company - Isle of Pines	305	1,582	32

(A) - Adjustment is the responsibility of the Audit Department witness.
(U) - Adjustment is the responsibility of the Utilities Department witness.

Dowd Water System's, Inc.
Isle of Pines and Emerald Shores Subdivisions
Explanation of Accounting and Pro Forma Adjustments
Test Year Ended December 31, 2000

Proposed Increase	(4)	(5)	(6)
Description	Service Revenue	Taxes Other Than Income	Income Taxes
	\$	\$	\$
(8) The Staff and the Company propose to record the effects of the proposed increase. The Staff's adjustment for "Taxes Other Than Income" differs from the Company's due to the Staff's use of a more up-to-date gross receipts factor. Income Taxes differ due to the differences in taxable income used by the Staff and the Company. (A&U)			
Per Staff - Combined	12,288	138	2,119
Per Staff - Emerald Shores	8,568	96	1,136
Per Staff - Isle of Pines	3,720	42	983
Per Company - Combined	12,288	138	1,476
Per Company - Emerald Shores	8,568	96	789
Per Company - Isle of Pines	3,720	42	687
Total Adjustments Per Staff - Combined	12,288	138	2,119
Total Adjustments Per Staff - Emerald Shores	8,568	96	1,136
Total Adjustments Per Staff - Isle of Pines	3,720	42	983
Total Adjustments Per Company - Combined	12,288	138	1,476
Total Adjustments Per Company - Emerald Shores	8,568	96	789
Total Adjustments Per Company - Isle of Pines	3,720	42	687

(A) - Adjustment is the responsibility of the Audit Department witness.
(U) - Adjustment is the responsibility of the Utilities Department witness.